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RIGHT OF A PROSPEROUS PRIVATE CORPORATION TO TRANSFER ITS ENTIRE PROPERTY AGAINST THE WILL OF A MINORITY OF THE STOCKHOLDERS.

A private corporation, it is sometimes said, which has no public duties to perform has generally implied power to alienate any or all of its property. With regard to railroads and other corporations that owe peculiar duties to the public, by reason of which they are clothed with the right of eminent domain and other privileges, a different rule prevails. It is well settled that these have no implied power to alienate their property, and thus possibly defeat the purpose of their incorporation. But the reason of this rule does not apply to trading or manufacturing corporations; and the transfer of the entire assets of such a company to another corporation, organized for the purpose of purchasing them, is one of the usual methods of reorganization. And in the formation of trusts for the purpose of controlling production or exchange, this is one of the methods by which a number of independent companies are combined into one, or by which a large corporation swallows up its smaller competitors. An analysis, therefore, of the leading American cases, together with some expressions of judicial opinion on this subject, may be of interest at this time.

While the question of monopoly and restraint of trade is sometimes discussed in the argument, the case is usually decided by a consideration of the question of corporate power alone. For a strictly private and prosperous corporation to sell its entire property, and thus render itself incapable of carrying on the business for which it was organized, is often said to be *ultra vires* the corporation. But if *ultra vires*, it is so in a modified way, in that the sale can be resisted or attacked only by a stockholder who has not assented to it, or a creditor who is injured thereby. The stockholders, in forming the corporation, agree with one another that the majority shall not exceed the corporate powers; and the creditor

may be supposed to have given credit to the corporation with the same understanding. The Supreme Court of California in *Miners' Ditch Co. v. Zellerbach*¹ said:

"An act is said to be *ultra vires* when it is not within the scope of the powers of the corporation to perform it under any circumstances or for any purpose. An act is also sometimes said to be *ultra vires* with respect to the rights of certain parties, when the corporation is not authorized to perform it without their consent; or with reference to some specific purpose, when it is not authorized to perform it for that purpose, although fully within the scope of the general powers of the corporation with the consent of the parties interested, or for some other purpose."

Therefore if all the stockholders consent, and no creditor's rights are prejudiced, the sale cannot be successfully attacked². The same result follows if the non-assenting stockholder has waived his rights, or is for any reason estopped to assert them.³ But the contract of sale, if not fully performed, may be repudiated by the selling company with impunity.⁴

The question proposed, then, is whether a non-assenting stockholder is entitled to have the sale enjoined, or rescinded when it has been consummated; or, in another aspect, *whether the majority have the right to make the transfer without the consent or acquiescence of every stockholder*—a question very inadequately treated by the text-writers.⁵

The question should be narrowed by leaving out of view such transfers when made by an *insolvent* or *unsuccessful* corporation. A corporation that is insolvent, or is doing an unprofitable business, has implied power, when acting by a majority, to sell its entire property and wind up its affairs, though some of the stockholders should object. The majority cannot be compelled to go on at a loss.⁶

Assuming, then, for the sake of orderly discussion that, under some circumstances, such a transfer by a prosperous trading or manufacturing corporation will be upheld, though opposed by a

¹ 37 Cal. 543; 99 Am. Dec. 300, with full note on the question discussed in this paper.

² *Holmes & G. Mfg. Co. v. Holmes & W. Metal Co.*, 127 N. Y. 252, 34 Am. St. Rep. 448; *State v. Western &c. Canal Co.* (Kan.), 10 Am. St. Rep. 166; *Morrisette v. Howard* (Kan.), 63 Pac. 756.

³ *Post v. Beacon etc. Electrical Co.*, 84 Fed. 371; *Campbell v. Argenta &c. Co.*, 51 Fed. 1.

⁴ *Easun v. Buckeye Brewing Co.*, 51 Fed. 156; *Mallory v. Hanau Oil Works* (Tenn.), 8 S. W. 396.

⁵ See 4 *Thompson on Corp.* 4443; 5 *Id.* 6685; *Cook on Corp.* 656, 662, 667; *Elliott on Private Corp.* 485.

⁶ *Price v. Holeomb* (Ia.), 56 N. W. 407.

minority of the stockholders, let us notice several limitations which the courts have placed upon the power.

1. *Transfer to a foreign corporation*—A corporation has no power to transfer its entire assets to a foreign corporation when the principal object of the transaction is to reorganize under the laws of another State, in order to obtain some real or supposed advantage afforded thereby. The courts do not permit the non-assenting stockholders to be deprived of the safeguards of the law under which they have chosen to organize.

Forrester v. Boston etc. Mining Co.,⁷ decided by the Supreme Court of Montana in 1898, was a case of this kind. A prosperous Montana company determined to transfer its entire property to another corporation which was to be organized under the laws of New York, taking in return therefor the stock of the new company, with the intention of distributing it among its own stockholders. It was provided that any stockholder who should be unwilling to take stock in the new company might receive instead a certain sum of money. The reasons given for the change were, that the great majority of the stock was held in the East, and it was therefore inconvenient to hold meetings in Montana; and also that the books of the company were required to be kept in Montana, while the stock was sold in the Eastern cities, and it was therefore inconvenient to make the transfer of the stock upon the books. The sale was enjoined at the suit of a minority stockholder, although he had acquired his stock after the sale had been made by the board of directors, and a meeting of stockholders called to ratify it.

This limitation, forbidding a sale to a foreign corporation, is often found coexisting with the one to be mentioned in the next paragraph, which forbids a corporation to invest in the stock of another corporation. In *McCutcheon v. Merz Capsule Co.*,⁸ a Michigan company entered into a contract with another corporation and two partnerships with a view to forming a gelatine capsule trust to be organized as a New Jersey corporation. The Michigan company was to transfer its entire property to the New Jersey company, taking a part of the stock of the latter. The Michigan company afterwards repudiated the sale. The New Jersey company, having been organized, sought to take possession by force; and suit was brought to restrain it from committing trespasses on the Michigan company's property. The defendant filed a cross-

⁷ 55 Pac. 229; rehearing denied, Id. 353.

⁸ 71 Fed. 787; 31 L. R. A. 415.

bill, seeking the enforcement of the contract. Without discussing the question of monopoly and restraint of trade, the court decided that the Michigan company had no power to make such a transfer. The statutes of Michigan, as it appears, safeguard the public and the stockholder by requiring reports to be published at stated intervals, showing the character of the corporate business, such as the amount of its capital stock, the amount of debts and assets, and a list of its stockholders. It was pointed out also that these provisions were not found in the New Jersey statutes. The reasoning of the opinion shows that the court thought it would be contrary to a sound public policy to permit corporate burial in Michigan in order to resurrection as a tramp corporation from New Jersey.⁹

2. Receiving stock of another corporation in payment—The second limitation to be noticed is, that a corporation has no power to transfer its entire assets to another corporation, and take in return the stock of the latter *to be held as a permanent investment*. This accords with the familiar rule of the common law that a corporation may not purchase the stock of another corporation, except in satisfaction of a debt or in the course of its legitimate business. By such a transaction the funds of a stockholder in the selling company would be invested in a new business, and he would gain or lose according as that business was successful or not; and yet that new business would be carried on under a different charter and different by-laws, in forming which he had had no voice, and under the direction of officers not accountable to him. Into such an arrangement he cannot be taken against his will. It is also considered contrary to public policy to permit a corporation to be formed within a corporation, the old one having delegated all its duties to the other, and continuing in existence as an empty shell merely for the purpose of collecting dividends and distributing them among its stockholders.¹⁰ Hence a sale of this kind has been set aside at the suit of a non-assenting stockholder, though made in good faith by a corporation that was doing an unprofitable business, and though the arrangement was shown to be advantageous to the stockholders of the selling company.¹¹

⁹ *People v. Ballard* (N. Y.), 17 L. R. A. 737, 1892; *Easun v. Buckeye Brewing Co.*, 51 Fed. 156; *Small v. Minneapolis &c. Co.* (Minn.), 47 N. W. 797; *Taylor v. Earle*, 8 Hun. 1. See *Abbot v. American &c. Co.*, 33 Barb. 578.

¹⁰ *McCutcheon v. Merz Capsule Co.*, *supra*, and cases cited in last note.

¹¹ *Byrne v. Schuyler &c. Mfg. Co.* (Conn.), 28 L. R. A. 304, 1895 (containing a good discussion of the question.)

*Hodges v. New England Screw Co.*¹² is sometimes cited as a contrary authority. That case was decided in 1850, when the jurisdiction taken by courts of equity over corporations was less extensive than at present. The court disposed of the questions before it without passing upon the validity of the transfer; it expressly declined to do this. The court held that it had no authority to compel the corporation to sell the stock thus acquired; but that the sale, when made, was valid.¹³

But it may be that the stock of the purchasing company in such a transaction may be taken by the selling company to be held *not as a permanent investment, but to be distributed among its own stockholders*, the old company being virtually dissolved, and its members becoming members of the new one. In this case what is the right of a non-assenting stockholder? It is very clear that he should not be forced into the new company. This company may have been organized with different powers and for different purposes, which he may not approve, and to which he has not consented. He might say with the defendant in a certain classical breach of promise case, *Non haec in foedera veni*. Nor will he be put to his election whether he will sell his stock in the old company for what it will bring, or go into the new one. He is entitled to have the transfer enjoined or rescinded. *Elyton Land Co. v. Dowdell*¹⁴ is a case in point. Here a very prosperous land improvement and development company sold its entire property to another corporation, organized with like powers and also with power to construct and operate furnaces and railroads; and received in return the stock of the new company, with the purpose of distributing it among its own stockholders. No provision was made for paying to any stockholder who should be unwilling to go into the new company the price of his stock. This transfer was set aside at the suit of a non-assenting stockholder.¹⁵ The court said:

"It may be that a private corporation may sell out its entire property by and with the consent of less than all its stockholders, for the purpose of paying its debts, or for the purposes of dissolution and settlement; but when this is the purpose, it must be clearly understood, and the terms and conditions of the sale must be within the contractual relations between the corporation and its creditors or shareholders. There can be no presump-

¹² (R. I.), 53 Am. Dec. 624.

¹³ *Holmes & G. Co. v. Holmes & W. Co.* (*supra*.)

¹⁴ 113 Ala. 177, 59 Am. St. Rep. 105 (1896).

¹⁵ See also *Gardner v. Hamilton*, 33 N. Y. 421; *Lauman v. Lebanon etc. R. Co.*, 30 Pa. St. 42.

tion that a creditor or stockholder of the dissolved corporation will accept in payment of his demand anything but money. He cannot be compelled to do so arbitrarily."

Still another variation of this transaction is presented when the stock is taken by the selling company to be distributed among its stockholders, and *provision is made for paying to a non-assenting stockholder the price of his stock* in the old company. In the cases to be cited here, the right of the majority to sell was established upon other grounds, and the only question was, whether they could compel a dissenting stockholder to part with his stock at their own valuation. An arrangement of this kind was sustained in *Treadwell v. Salisbury Mfg. Co.*,¹⁶ decided by the Supreme Court of Massachusetts in 1856. According to the terms of that arrangement, if any stockholder refused to accept the stock, it was to be sold and the price given to him. The court was, no doubt, satisfied that the non-assenting stockholder would thus receive a fair equivalent for his stock in the old company.

But in *Mason v. Pewabic Mining Co.*,¹⁷ decided by the United States Supreme Court in 1890, a different rule was announced. In this case the property was valued by the majority at a certain sum, and transferred to a new company, both companies being controlled by the same persons; and any stockholder who would not accept the stock of the new company was to get his proportionate share of that sum. The court held that a minority stockholder could not be compelled to relinquish his right in the company's property at a price *arbitrarily fixed* by the majority. He was entitled to have the property sold to the highest bidder at a public sale, the amount offered by the majority being regarded as the first bid. In this case the majority had the right to insist upon a sale, since the company's charter had expired; but there would seem to be no doubt that, under this decision, the minority would in any case be entitled to demand a public sale to the highest bidder. This decision places an important qualification upon the right of the majority to sell.

The foregoing limitations go a good way toward denying the power of a private corporation, in prosperous circumstances, to transfer its entire property against the will of a minority of its stockholders; and beyond these limitations, the question apparently ceases to be a practical one, so far as the courts are concerned. Upon the whole, no case was observed, in an examination of the

¹⁶ 7 Gray, 393, 66 Am. Dec. 490.

¹⁷ 133 U. S. 50; 33 L. Ed. 524.

American authorities, in which the sale was upheld in the absence of any evidence to show that the exigencies of the company's business rendered it necessary. But it may be of some interest to quote from the opinions of various courts on both sides of the general question.

*Forrester v. Boston etc. Mining Co.*¹⁸ goes furthest, probably, toward denying the power. In this case the Montana court said:

"At common law, neither the directors nor a majority of the stockholders have power to sell or otherwise transfer all the property of a going, prosperous corporation, able to achieve the objects of its creation, as against the dissent of a single stockholder. This doctrine is thoroughly established by the authority of adjudged cases, and rests upon the soundest principles."

But the authorites cited do not sustain this proposition so broadly stated.

In *Byrne v. Schuyler etc. Mfg. Co.*¹⁹ the Connecticut court said:

"It seems to be the settled law of America and England that any act or proposed act of a corporation, or of the directors, or of a majority of the stockholders, which is not within the express or implied power of the charter of incorporation—in other words, any *ultra vires* act—is a breach of the contract between the corporation and each of the stockholders, and that consequently any one or more of the stockholders may object thereto, and compel the corporation to observe the terms of the contract set forth in the charter. Therefore it results that neither the directors nor a majority of the stockholders can sell the corporate property against the dissent of any stockholder. This is entirely clear in the case of a solvent corporation. And although the corporation is actually insolvent, if the purpose of the sale is not the *bona fide* winding up of its business, but is the continuance of the business in another corporation, the rule is not changed. A dissenting stockholder may interfere and prevent the sale."

On the other hand, in assertion of the power, the Supreme Court of Massachusetts said in *Treadwell v. Salisbury Mfg. Co.*:²⁰

"We entertain no doubt of the right of a corporation, established solely for trading and manufacturing purposes, by a vote of the majority of their stockholders, to wind up their affairs and close their business, if in the exercise of a sound discretion they deem it expedient so to do. At common law the right of a corporation, acting by a majority of their stockholders, to sell their property is absolute, and is not limited as to objects, circumstances, or quantity."

This case is sometimes cited as sustaining the right of the majority to sell, notwithstanding the dissent of the minority; but there was evidence that the company's financial condition rendered it necessary.

¹⁸ *Supra.*

¹⁹ *Supra.*

²⁰ *Supra.*

In the extract just given from *Byrne v. Schuyler etc. Mfg. Co.*, the right of the non-assenting stockholder to defeat the transfer is based upon his contract with the corporation; that is, upon the contract of all the stockholders with one another, which is implied in every charter. Is it agreed in this contract that the corporation shall continue for the statutory period, if not unsuccessful? And if so, is this such a contract as the courts will specifically enforce? The latter question could hardly be answered in the affirmative; and yet, as the cases cited show, the courts will exercise their moral suasion in that behalf by defeating an attempt to practically dissolve the corporation by transferring its entire property.

The question is sometimes settled by statute; in West Virginia the majority, it seems, have power to dissolve; in Iowa they have not. As to the existence of the right at common law, the New York court said in *People v. Ballard*:²¹

"A corporation cannot cease to exist of its own will. Its life continues until either the charter period has expired, or the court has decreed a dissolution. The law made it, and the law only can put an end to it. As it cannot take its own life directly, it cannot do so indirectly, for that would be a fraud upon the law and against public policy. By the transaction complained of, the defendant company was stripped of all its property, and thus prevented from going on in business, and deprived of all means of carrying into effect the object of its existence. While a corporation may sell its property to pay debts or to carry on its business, it cannot sell its property in order to deprive itself of existence."

And the New Jersey court said in *Kean v. Johnson*,²² which was an attempt to consolidate two railroad companies:

"That the majority should have the power claimed for them, does not seem to me to be the contract between the stockholders, for there is a contract, as already shown, in the case of every corporation, between them. That contract is that their joint funds shall, under the care of specific persons, generally called directors, be employed, and that for certain specified purposes. Sometimes the duration of such employment is limited in the charter, and then until that time it must continue so employed, unless, perhaps, in the case of clear loss. Sometimes no time is fixed by the charter at which the proposed use of the capital shall cease, and then the contract between the parties is, that so long as the affairs of the company are prosperous, it shall go on, unless all consent to the contrary."

Reference was made in the beginning of this paper to the bearing which this question has upon the formation of trusts. It may now be stated, in conclusion, that while the courts have practically

²¹ *Supra.*

²² 9 N. J. Eq. 414.

denied the power, they afford a very inadequate remedy against the formation of trusts, since no one generally can complain except a non-assenting stockholder, and a stockholder is rarely found who is disinterested enough to forego his share of the "gaineful pilladge" which a great combination can secure, in order to promote the general welfare.

In New York it has been held upon great deliberation, though with strong dissent, that a suit might be maintained by the attorney-general in the name of the State, under a system of legislation which showed a progressive tendency toward State supervision of corporations, to compel the trustees of a corporation to account for an unlawful disposition of the company's property, made with the consent of a majority of the stockholders.²³ But even here it was conceded that the State was to be regarded as the representative of those stockholders only who had not consented to the transfer.

Norfolk, Va.

GORDON PAXTON.

THE ADOPTION OF STATE CONSTITUTIONS IN THE UNITED STATES.

In view of the fact that the Virginia Constitutional Convention has under consideration the question of proclaiming or submitting the new Constitution, it seems peculiarly fitting at this time to examine the precedents which have been established in the cases of the 131 state constitutions adopted since 1776. For convenience in classifying the different constitutions, the years from 1776, when in accordance with the recommendation of Continental Congress the colonies adopted their constitutions, to 1902 may be divided into three periods: the first period extending from 1776-1830; the second from 1830 to 1860, inclusive; and the last from 1861 to 1902.

I.

(1776-1830.)

(a) *Submitted*—In the first period, 1776-1830, the constitutions submitted to the vote of the people are as follows:

Constitution of Connecticut, 1818; Maine, 1820; Massachusetts,

²³ *People v. Ballard (supra)*.